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FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

Kenneth Rust
Director,
Federal Regulatory Matters

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NYNEX

March 3, 1995

Ex Parte

Mr. William F. Caton
Acting Secretary
Federal Communications Commission
1919 M Street, N.W. - Room 222
Washington, D.C. 20554

Re: CC Docket No 94-1

Dear Mr. Caton:

Attached is a NYNEX filing in the above-referenced docket. The original and a copy of this *ex parte* notice are being filed in the Office of the Secretary. Please include it in the public record of this proceeding.

Respectfully submitted,

Ken. Rust

Attachment

cc: Office of Chairman R. Hundt
Office of Commissioner A. Barrett
Office of Commissioner R. Chong
Office of Commissioner S. Ness
Office of Commissioner J. Quello
K. Wallman
R. Metzger
M. Katz
M. Uretsky
J. Wall

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FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, DC 20554

In the Matter of	)	
	)	
Price Cap Performance Review for Local Exchange Carriers	)	CC Docket No. 94-1
	)	

A NYNEX PROPOSAL FOR THE LEC PRICE CAP PLAN

Introduction

In *ex parte* contacts with the FCC on December 28, 1994, January 6, January 13, and January 17, 1995, NYNEX put forth the notion that the elimination of sharing be linked with local exchange competition. NYNEX also advanced this position in its filing on the proposed USTA plan submitted January 31, 1995. The rationale underlying the NYNEX proposal has to do with the benefits that accrue to the public and to participants in a competitive environment. NYNEX herein amplifies its original proposal by providing greater specificity as to how the Commission should encourage local exchange carriers to take on the challenges and reap the benefits of a competitive local exchange marketplace[1]. The steps NYNEX proposes can lead to the creation of a fertile environment for local exchange competition, and the presence of such an environment ought to assure the Commission that the economic infirmities of the price cap sharing mechanism can be dispensed with. The criteria set forth below, when met, will mean that local exchange competition

[1] The structure of the January 18, 1995 USTA proposal suggests that the Commission could impose a high productivity hurdle for LECs wishing to gain the benefits of "pure" price cap regulation, and retain a lower one for LECs unable or unwilling to attempt the challenge of a higher productivity factor. Sprint presents a similar position in its February 2, 1995 *ex parte* in CC. Dkt. No. 94-1. Having a high productivity factor as the basis for the elimination of sharing, however, sends an incorrect public policy message, and ironically allows only those firms with high productivity expectations to opt for a "no sharing" regime that will encourage them to be even more efficient. For firms opting for a higher productivity factor in order to eliminate a sharing obligation, however, becoming more efficient will mean increasing the usage on the network, and such firms will not want to open their markets to local exchange competition -- a fundamental Commission policy objective -- because competition can reduce network usage in the short term.

is truly viable; they will not mean that competition is sufficiently robust to warrant the elimination of all regulation, either under a price caps regime or traditional ROR regulation, but a LEC meeting the criteria will be well on its way to the fully competitive marketplace that warrants limited regulation[2].

Background

The Commission, through a long series of Orders, has taken steps to remove restrictions to competition in interstate markets. It has done this because a competitive market is the best mechanism to control price and prompt companies to deploy modern infrastructure in a rapid manner. These policies can be hindered, however, if restrictions exist to prevent similar competition in intrastate markets[3]. For example, a competitive access provider (CAP) who can use expanded interconnection arrangements only to provide interstate access, because the arrangement is not available in the intrastate jurisdiction, may determine that that geographic area is not an attractive one in which to offer competition to the incumbent LEC. Both the Administration and Congress have expressed positions that support the development of competition in the local telecommunications markets.

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[2] The advantages of a competitive local exchange marketplace have been noted by various parties in this proceeding. The Ad Hoc Telecommunications Users Committee (Ad Hoc), for example, observed that "Because private risk capital and market-based decision making represent the best way to efficiently allocate resources in a market economy, the Commission can most effectively assist in the development of a ubiquitous national information infrastructure by continuing its laudable efforts to promote competition in the local infrastructure." Comments of the Ad Hoc Telecommunications Users Committee in the Matter of Price Caps Performance Review for Local Exchange Carriers (CC. Dkt. No. 94-1), pp.10-11 (May 9, 1994). The advantages of local exchange competition as an impetus toward greater efficiency and infrastructure deployment were stated again by the representatives of the Consumer Federation of America (CFA), Sprint, and Ad Hoc during the large *ex parte* meeting held recently by the Commission on March 1, 1995.

[3] The International Communications Association (ICA) pointed out a similar situation in its Reply Comments in this proceeding. ICA observed, "A significant barrier to competition is the current inability of entrants to offer, or users to buy, combined interstate access and local services due to state-level prohibitions." Reply Comments of the International Communications Association in the Matter of Price Cap Performance Review for Local Exchange Carriers (CC. Dkt. No. 94-1), p. 7, (June 29, 1994)

In a statement before the House Subcommittee on Telecommunications and Finance on May 26, 1994, Chairman Hundt said:

> ... the enormity of the tasks before the Commission is reflected in a number of areas where technology and investment have made change possible. In the common carrier area, for example, the Commission has sought to bring competition to all aspects of telephone service. Its proceedings to provide expanded interconnection access capability go beyond long distance and include local exchange competition. Ensuring the substantial benefits of greater consumer choice, faster deployment of technology, reduced rates, and increased efficiencies on the part of the local exchange carrier require considerable efforts of the agency.[4]

Proposal

NYNEX shares the Chairman's belief that competition provides the greatest incentives for increased efficiency and prompt infrastructure deployment. The strongest argument for the elimination of sharing is also based on the greater incentive for efficiency it brings with it, and so the elimination of sharing combined with a competitive local exchange market can yield twofold public benefits. It is appropriate, therefore, that the Commission link the two by taking steps now to encourage LECs to open up their local exchange markets. To this end, and considering the controversy surrounding the various proposals for establishing an appropriate productivity factor, NYNEX suggests that the Commission retain the present productivity (X) factor (i.e., 2.8% + 0.5% Consumer Productivity Dividend) while it assures itself of the efficacy of the Total Factor Productivity (TFP) approach espoused by USTA . Even while it undertakes the potentially protracted examination required to evaluate the various proposals, including USTA's, it can establish the appropriate incentives for LECs by adopting the "expanding sharing bands" approach put forth below. Once the Commission has had the opportunity to confirm that the USTA position ought to be adopted in establishing the TFP on an on-going basis, it can substitute the new factor but retain the sharing bands concept.

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[4] "Statement of Reed E. Hundt, Chairman, Federal Communications Commission, Before the Subcommittee on Telecommunications and Finance, Committee on Energy and Commerce, House of Representatives, Concerning The 1995 Authorization Act For The Federal Communications Commission", p. 4 (May 26, 1994).

NYNEX suggests that the Commission establish in this phase of the price cap review proceeding a series of "sharing bands" around the 11.25% authorized ROR that will allow LECs to retain more of their efficiency gains as each implements certain steps designed to foster and support the growth of local exchange competition in its operating territory. These suggested steps are listed below and summarized in the attached chart.

- The base-line situation assumes that no competition is allowed in states comprising the LEC operating territory, and that no intrastate collocation tariffs have been approved. Under such operating conditions a LEC would have to share 50% of its interstate earnings above 11.75%, and all of its interstate earnings above 13.75%. The LFA threshold would be 10.75%.

- The next sharing/LFA bands would apply when 30% of the access lines in the operating territory are covered by states having approved local exchange competition, the LEC having had tariffs approved to provide unbundled local loops, and the LEC either having had tariffs approved or having made available through contracts intrastate expanded interconnection arrangements and number portability options for use by competitors. Under such conditions a LEC would share 50% of its interstate earnings above 12.25% and all of its interstate earnings above 16.25%, and the LFA threshold would be lowered to 10.25%.

- When 80% of the LEC access lines in its operating territory are affected by the above criteria, a LEC will only have to share 50% of its interstate earnings above a 13.25% level, and all of its interstate earnings above a 18.25% level. At that point the LFA threshold will be at 9.25%.

- In the final stage of moving to "pure" price cap regulation, a LEC will not have to share any of its interstate earnings, and there will be no LFA trigger. The final stage is reached when, in addition to the criteria above having been met, states have authorized competing local exchange carriers (CLECs) to compete against the incumbent LEC, CLECs have been assigned telephone numbers in the same manner as the LEC, mutual compensation arrangements have been negotiated for exchange of traffic between CLEC and LEC networks, and either through tariff or contract the CLEC has available to it arrangements that address interconnection of networks and access to Directory Assistance and E911/911 data bases. In addition, 40% of the business lines or 60% of interstate access revenues (Switched and Special) in the LEC operating territory must be in wire centers in which CLECs provide competition to the LEC through either the use of expanded interconnection arrangements, deployment of facilities, or announced plans to offer service within the geography.

Conclusion

The NYNEX proposal offers two advantages. First, by tying the elimination of sharing directly to efforts to foster and support local exchange competition, the NYNEX proposal provides needed incentives for LECs to accept local exchange competition and achieve the efficiency gains and infrastructure deployment imperatives that accompany it. Second, it eliminates the need to establish immediately a new X factor, which simplifies the Commission's task in sorting through the competing arguments for and against various X factors, while still protecting the public interest.

The Commission should act now to create opportunities for local exchange competition by adopting the NYNEX proposal. If the Commission shares NYNEX's view that the greatest incentives for LEC efficiency gains and infrastructure deployment will come from a fully competitive environment, the NYNEX proposal must be viewed as an innovative solution to the problem of finding a way to prompt LECs with a short term view to see the long term benefits of competition.

Attachment

NYNEX Price Cap Proposal

Productivity Factor	LFA	Sharing Range		Trigger
		50/50	100	
3.3	10.75	11.75 - 13.75	>13.75	
3.3	10.25	12.25 - 16.25	>16.25	30% of Access Lines in Operating Territory meet Criterion 1
3.3	9.25	13.25 - 18.25	>18.25	80% of Access Lines in Operating Territory meet Criterion 1
3.3	None	None		In addition to above, 40% of business lines or 60% of interstate access revenues in Operating Territory meet Criterion 2

Criterion 1

- State Commission removes restrictions preventing local exchange competition.
- LEC has tariffs in place that unbundle and make available to competitors the local loop.
- LEC either has tariffs or makes available through contracts the following:
  - Intrastate use of interstate expanded interconnection arrangement;
  - Number portability options for use by competitors.

Criterion 2

- State commissions have certificated other carriers - competing local exchange carriers (CLECs) - to compete against incumbent LEC.
- CLECs have been assigned telephone numbers in the same manner as the LEC.
- Either through tariff or contract, the CLEC has available arrangements that address:
  - Interconnection of networks
  - Access to directory assistance and E911, 911 database
  - Mutual compensation arrangements for termination of traffic on competing networks.
- CLECs provide competition to the LEC within a wire center through either use of expanded interconnection arrangements, deployment of facilities or announced plans to offer service within the geography.